The Construction Network

November 2020

OEI

OFFICE OF EXTRAORDINARY

INNOVATION

Metro

How
Public-Private Partnerships
Can Deliver Value for Metro

Which is a P3?

Metro ExpressLanes DBOM

CNG Bus Fueling

Contracted Bus Service

Metro's Advertising Contract

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Public-Private Partnerships (P3)

We All Know What a P3 Is, Right?

> **Collaboration** between a public agency and a private company to **deliver a public service or facility**

> Each party **shares its key skills** and takes on the risks it is **best able to manage**, leading to benefits such as cost savings and project acceleration

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What it is, What it isn't

What it is / does

- A P3 can leverage the private sector's skills and financing
- A P3 can provide a mechanism to share in the risks and rewards of a project
- A P3 could incentivize innovation and long-term performance

What it is not / does not do

- A P3 is not a new source of revenue
- A P3 does not change the ownership of the assets; Metro will retain the ownership
- A P3 model does not necessarily suit all projects

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Why Public Private Partnerships?

But *Why* use a Public-Private Partnership?

> Private-sector expertise, innovation, & rigor

> Certainty, risk, and performance

> Whole-of-life cost considerations

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Metro P3 Principles

> - Public interest is paramount – The top priority is securing greater value than a fully public approach
> - Value for money must be clear – The *actual financial value* of the P3 must clear, compared to a public model
> - Process must be fair and transparent – Appropriate documentation, public notice and comment, full competition
> - Public ownership and control – Private role is limited by public ownership and oversight with clear accountability mechanisms

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Common P3 Misconceptions

> P3s **DO NOT privatize public resources**. The public retains ownership and oversight of their investments.

> P3s **DO NOT lead to public sector job losses**. Any Metro P3 must meet state and county workforce standards, and be governed by Labor agreements.

> **Public services DO NOT take a backseat** to private sector profits. Projects and performance agreements are designed to maximize public benefit.

> Smart P3s **DO NOT exclude small and local contractors**. P3s can and do include SBE and DBE requirements.

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Metro Procurement Approaches

Metro has prior experience with several procurement models including DB, DBOM, and DBF (explored for Gold Line).

> Why would Metro consider new delivery models beyond DBB and DB?

> Why would Metro consider private involvement in transit operations and maintenance?

Metro Regional Connector
DB

Metro ExpressLanes
DBOM

Gold Line
DBF

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Potential P3 Benefits

> **Faster Project Delivery Timeframes**

Accelerate construction of high priority projects by compressing and overlapping project sequences

> **Allows Greater Creativity & Technology Access**

Use of advanced technologies or proprietary methods that are not generally available through standard procurement

> **Creates New & More Flexible Access to Financing**

New sources of private debt and equity can be structured to be more flexible and minimize costly project risks

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Potential P3 Cost Savings

> Construction & Life-Cycle Cost Savings

Minimizes schedule and cost overruns and creates incentives for cost savings over the life of the project

> Shifts Risks & Costs to Private Partner

Private assumption of project risks leads to more effective management and shields the public from potential costs

> Improves Project Performance

Performance and accountability for complex project tasks with built in financial incentives and penalties

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How is Value *Actually* Delivered?

> **Integrated Project Scope**
>
> Opportunities for design and implementation efficiencies

> **Performance Based Contract**
>
> Performance requirements vs. technical specifications

> **Skin in the Game**
>
> Private partner contributes financial equity, which is at risk over the life of the project

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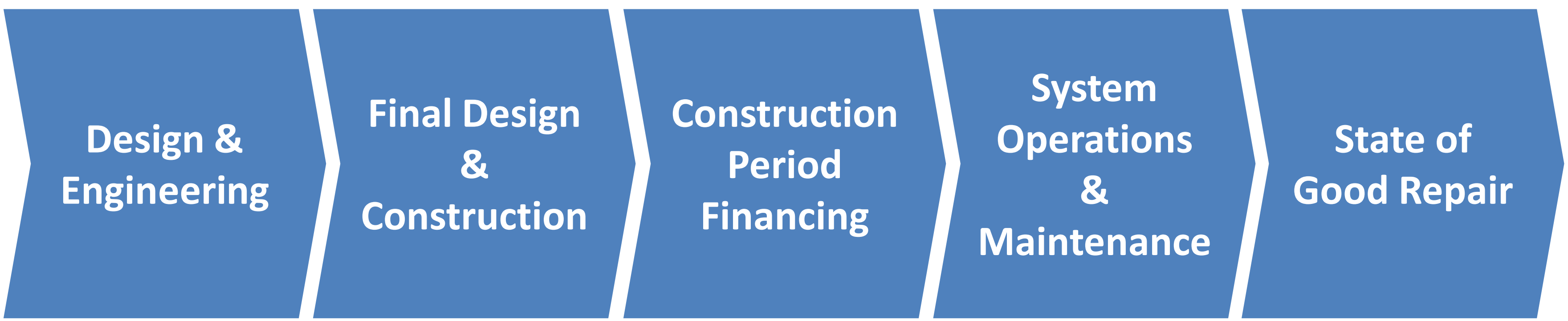
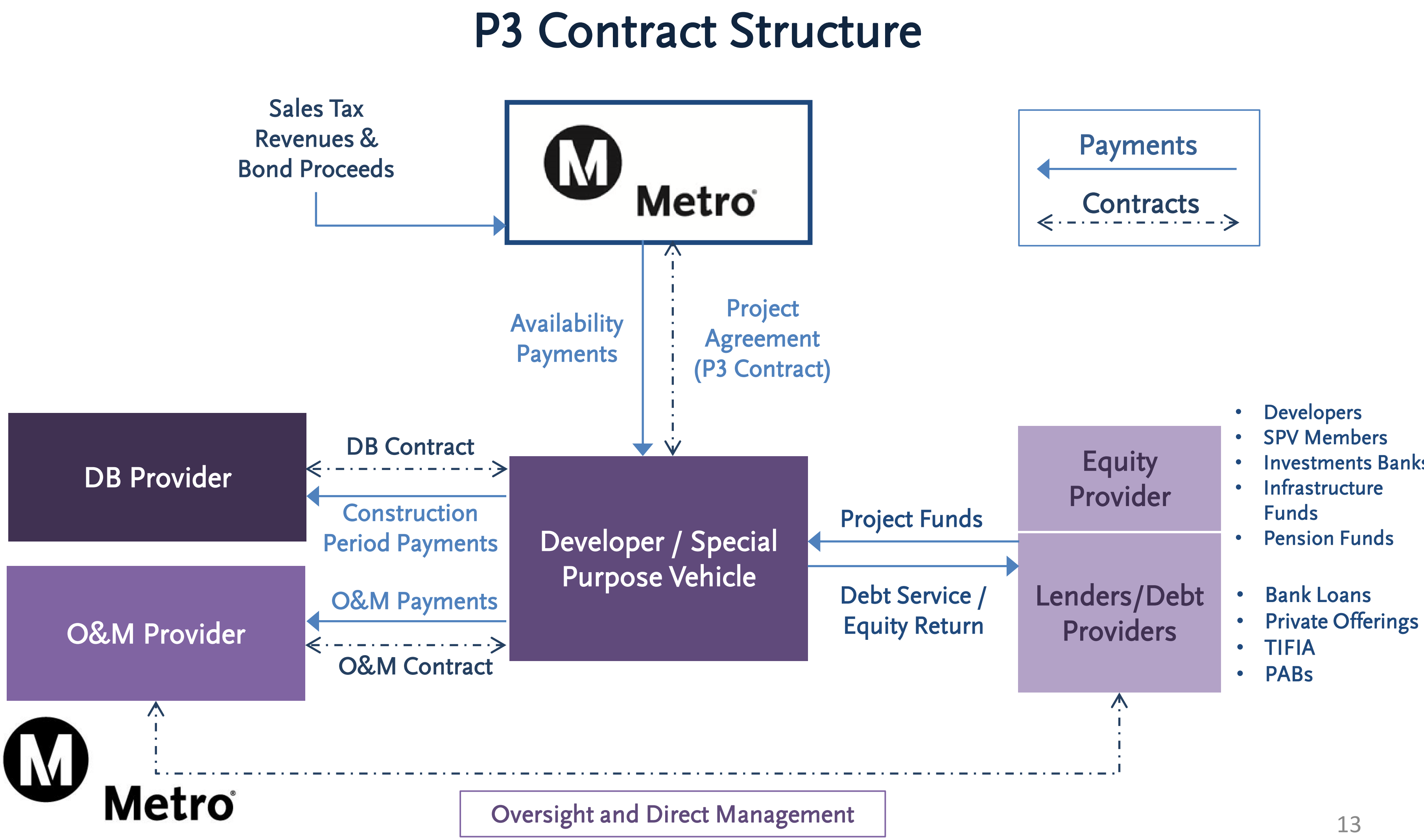
Integrated Project Scope

Typical Private Sector Roles in a DBFOM

- Project design/engineering
- Financial/cash flow
- Construction and project management
- System performance during operations
- Facility management and long term maintenance



Impact of Contract Structure



Capital At-Risk

> **The Value of <u>Capital At-Risk</u>:** When a private firm invests its own equity into a project, it creates incentives for the firm to ensure **<u>long-term quality & performance</u>** as capital is repaid

$1 Billion Capital Project

Traditional Delivery	
$400,000,000	• Metro Cash & Grant Funds
+ $600,000,000	• Sales Tax Bond Proceeds, repaid via debt service
$1,000,000,000	Total Capital Cost

Public-Private Partnership	
$400,000,000	• Metro Cash, Grants, & Sales Tax Bond Proceeds
$550,000,000	• Private Debt Proceeds (Bank Loans, Private Debt), repaid via Availability Payments
+ $50,000,000	• P3 Equity, repaid via AP after P3 Debt
$1,000,000,000	• Total Capital Cost

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P3 Incentivizes Performance

> Metro makes Availability Payments to the Developer when the facility is "available" for regular use, and if predetermined performance standards are met.

SATISFACTORY PERFORMANCE

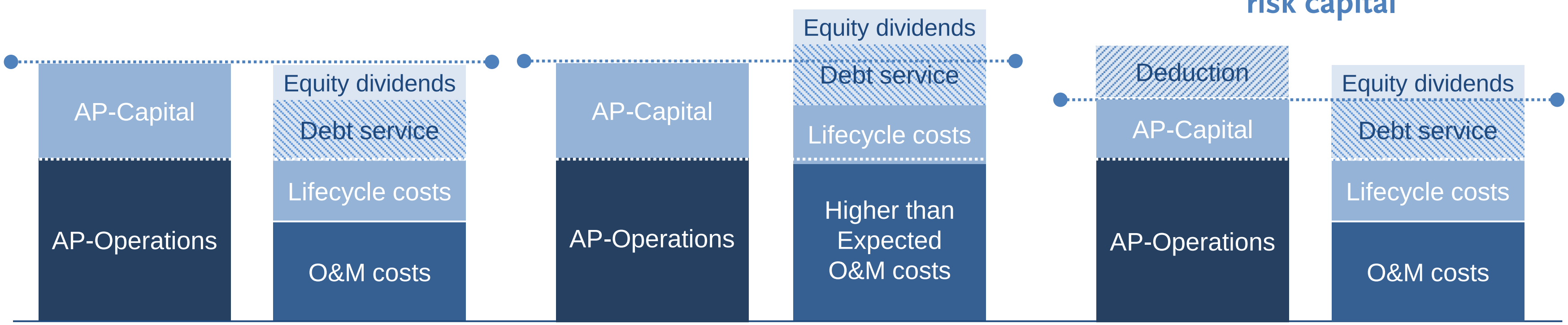
Developer uses APs to secure financing for O&M costs and construction cost repayment

COST OVERRUN

Absorption of cost overrun by providers of at-risk capital (equity & debt) incentivizes quality performance

POOR PERFORMANCE

AP performance deduction due to noncompliance incentivizes quality performance through at-risk capital



Maximum Availability Payment

Developer's Budget

Developer Uses of Funds

No Stress

Costs Exceed Maximum Payment

Developer Uses of Funds

Reduction to Equity Dividend and Threat to Debt Repayment

Reduced AP for Non-Compliance with Performance Standards

Developer Uses of Funds

Reduction to Equity Dividend and Threat to Debt Repayment

P3 Business Case Development Process

Step 1 – **Project Screening & Selection**

Projects identified through evaluation of Unsolicited Proposals or internal staff screening

Step 2 – **Qualitative Project Assessment**

Project characteristics evaluated for key risks & opportunities

Requires a project concept alternative & major project characteristics to be defined

Step 3 – **Market Sounding**

Interviews of P3 industry participants to evaluate potential market interest & gather information about project risks & opportunities

Step 4 – **Project Cost Report**

Initial project Lifecycle Cost Report covering construction, O&M, & rehabilitation/SGR

Requires project level of design minimum of 5-10 percent. Greater design desirable for more complex or risky projects

Step 5 – **Project Risk Assessment**

Project's risks across all lifecycle phases identified & evaluated

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P3 Business Case Development Process

Step 6
Value-for-Money & Financial Analysis

Delivery of the project is compared under Design-Build & P3 scenarios to determine which offers the best value

Analysis of key value drivers & optimal financial structuring.

Step 7
Project Funding & Affordability Assessment

Project costs & cashflows under Best-Value delivery method are compared to available funding

Requires final project funding plan.

Step 8
Recommend Best-Value Procurement Strategy

Final procurement strategy established for Best-Value delivery method of final project scope

Requires selection of Locally Preferred Alternative

Step 9
Final Project Performance Specs

Performance & technical specifications for each stage of the project are finalized

Step 10
Draft P3 Procurement Package

Final P3 RFQ and RFP issued

Requires completed NEPA/CEQA, & funding to be identified.

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Metro Potential P3 Projects

Metro has two projects under development as a P3

1. Sepulveda Transit Corridor (Pre-Development Agreement)
2. West Santa Ana Branch LRT P3

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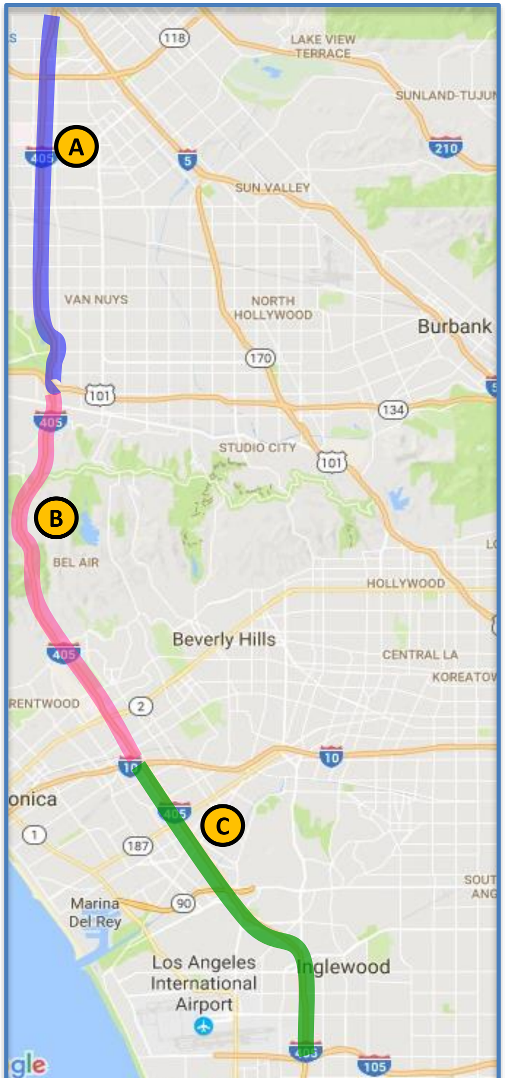
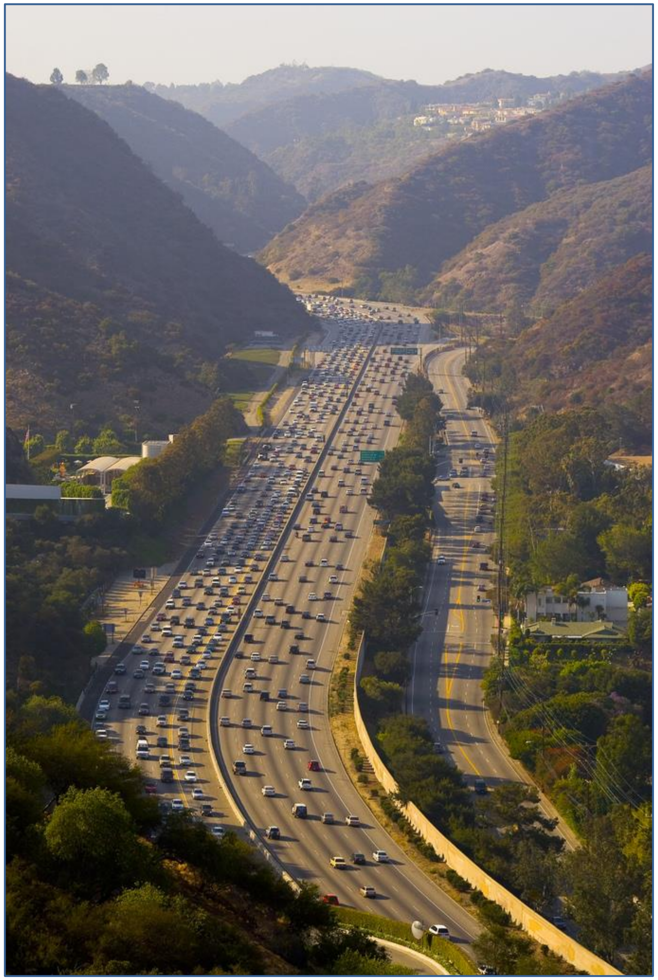
Sepulveda Pass Corridor Project



- Metro planned delivery: Managed lanes through Sepulveda pass; New rapid transit connection between Van Nuys/Orange Line BRT and Purple/Expo Rail Transit, eventually extended to LAX
  - $9.8 billion total funding; $5.7 for Valley-Westside transit
  - Managed lanes groundbreaking in 2024, delivery in 2026; 2033 delivery of Valley-Westside transit; 2048 delivery of Westside-LAX transit
- Unsolicited Proposal analysis supports P3 transit delivery
  - UPs indicate significant opportunities for innovation to optimize project delivery, cost, and performance
  - Early contractor involvement to support balancing of constructability, performance, affordability, and project risk
- No significant projected P3 benefit to Metro for Managed Lanes element, compared to baseline approach

Pre-Development Agreement

- **P3 Project to be Developed via a Preliminary Development Agreement (PDA)**
  - PDA offers right of first negotiation to construct (and operation/maintain) upon achievement of project feasibility (some work at-risk)
  - “Off-ramps” with technical work products at various development stages
- **Factors supporting use of PDA**
  - Given complexity, size and current status, a PDA approach could allow Metro to more efficiently develop and refine a feasible scope
  - Supports balancing of all project goals (access, ridership, throughput, travel time savings, etc.) with affordability limitations and project risk
  - Could help accelerate overall project delivery



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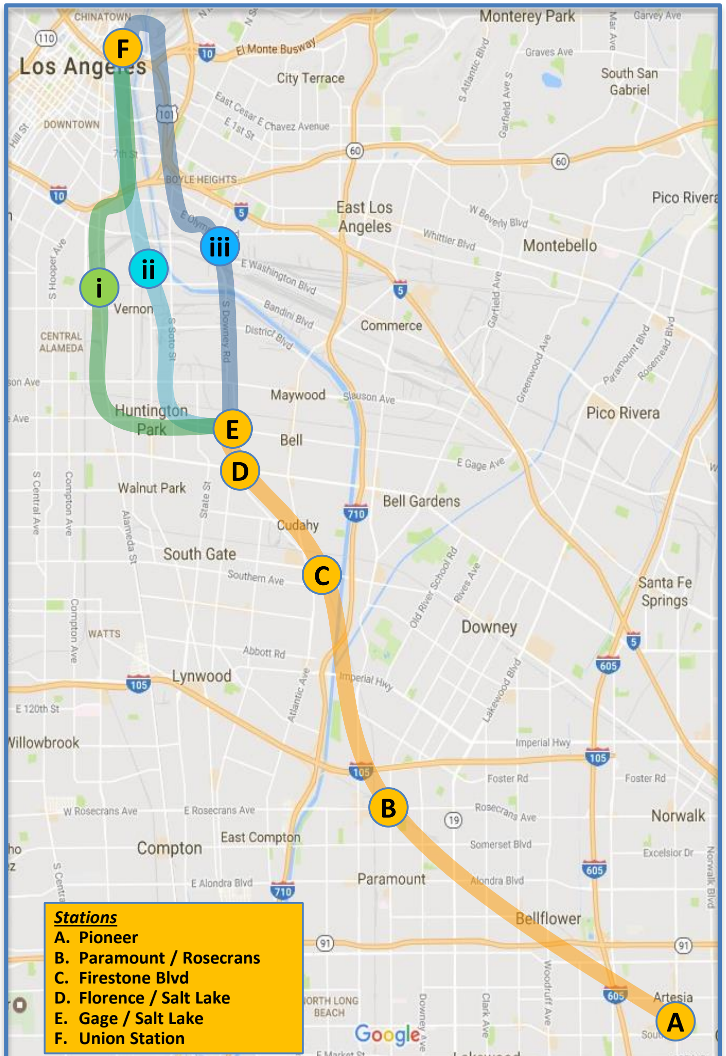
West Santa Ana Branch LRT



- > **Metro planned delivery: LRT delivered in two phases, working south to north**
  - $4 billion ($2015) Measure M funding allocation
  - Groundbreaking in ~2022; Delivery in ~2028 (Phase I) & 2041 (Phase II)
- > **Unsolicited Proposal analysis supports P3 delivery**
  - Metro received proposals for different P3 models, both of which combine phases and show evidence of potential cost savings and project acceleration
  - Outstanding affordability challenges due to early operations & complex scope, compounded by programmed cash flows
- > **Innovative procurement to incorporate scope and phasing**
  - > Variable project scope to maximize acceleration within funding constraints

Thank You

Questions?

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